CANADA

NATIONAL ENERGY BOARD
REASONS FOR DECISION

Trans-Northern Pipelines Inc.

Application dated 11 March 1987
for new tolls effective 1 February 1987

RH-3-87

July 1987

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Recital and Submittors

IN THE MATTER OF the National Energy Board Act and the Regulations made thereunder; and

IN THE MATTER OF an application by Trans-Northern Pipelines Inc. made under Part IV of the Act for an order respecting tolls and tariffs, filed with the Board under File No. 1762-T2-9.

Before:

R.F. Brooks	Presiding Member
J.R. Jenkins	Member
R.B. Horner, Q.C.	Member

Submittors:

W.J. Greer	Trans-Northern Pipelines Inc.
R.S. O'Brien, Q.C.	Air Canada, Canadian Airlines International Ltd.
C.C. Black	TransCanada PipeLines Limited

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Abbreviations and Definitions

Airlines	Air Canada/Canadian Airlines International Ltd.
Base Year	1 January to 31 December 1986
Board/NEB	National Energy Board
Company/ Trans-Northern	Trans-Northern Pipelines Inc.
DCF	Discounted Cash Flow
Dominion Securities	Dominion Securities Inc.
Dorval	Dorval International Airport
Long-Canada	Long-Term Government of Canada Bond
m^3	Cubic Metre
m^3km	Cubic Metre-Kilometre
Mirabel	Mirabel International Airport
Pearson	Lester B. Pearson International Airport
Test Year	1 January to 31 December 1987
1981 Decision	"National Energy Board Reasons for Decision in the matter of an Application by TNPL Inc. under Part IV of the National Energy Board Act (Toll Application) December 1981"
1985 Decision	"National Energy Board Reasons for Decision in the Matter of an Application by Trans-Northern Pipelines Inc. under Part IV of the National Energy Board Act (Toll Application) May 1985"
13-Point Average	An average determined by aggregating the balance at the opening of a year and the balances at the end of each month of the year, and dividing by thirteen. Over the years, the Board and others have referred to an average determined in this fashion as a 13-month average.

Note: All dollar amounts have been rounded to the nearest thousand. Totals may not add due to rounding.

Overview

(Note: This overview is provided solely for the convenience of the reader and does not constitute part of this Decision or the Reasons, to which readers are referred for the detailed text and tables.)

The major decisions of the Board with respect to the Trans-Northern toll application are summarized below.

Revenue Requirement

The revenue requirement for the 1987 test year was forecast by Trans-Northern to be $25.1 million, about $1 million in excess of that previously approved by the Board for the January to December 1985 test year. Among other things, the Board has determined that the revenue resulting from inter-refinery transfers should be included in the determination of the revenue requirement, resulting in a reduction of the requested amount. The net effect of the Board's decisions reduces the applied-for revenue requirement by $.4 million, resulting in an approved amount of $24.7 million.

Cost of Capital

The Board has approved a rate of return on equity of 13.75% compared to the 14.75% requested by the Company. It has also accepted the applied-for cost rate of 10.25% associated with the Company's proposed debt re-financing. As a result of its decisions in this proceeding, the approved capital structure is comprised of 49.08% debt and 50.92% equity, and the authorized rate of return on rate base is 13.29%.

Throughput

The Board has approved a throughput forecast of 8 194 000 cubic metres. This forecast reflects acceptance of the Company's estimates of deliveries to all locations except Dorval and Mirabel airports, for which the Board finds the Airlines' estimates, with which Trans-Northern agreed, to be reasonable.

Toll Design

The Board has directed Trans-Northern to refund to its shippers the excess revenue it collects while interim tolls are in place, together with carrying charges. The refund is necessary because the tolls resulting from this Decision are less than the interim tolls which have been in effect since 1 February 1987.

Chapter 1
Application

By letter dated 21 January 1987, the National Energy Board (the Board or NEB) issued Order No. TOI-1-87 to implement interim tolls effective 1 February 1987 and directed Trans-Northern Pipelines Inc. (Trans-Northern or the Company) to file certain cost of service, throughput, rate of return and income tax information.

The Company filed a Class 3 application dated 11 March 1987 for new tolls pursuant to Part IV of the National Energy Board Act.

Trans-Northern's proposed tolls were based on a 1987 test year and were designed to recover a total revenue requirement slightly over $25 million. This total included, among other things, an overall rate of return of 13.81% on a rate base of $36.5 million. This application was addressed by written submission.

Chapter 2
Revenue Requirement

A summary of the approved revenue requirement for the test year ending 31 December 1987, together with Board adjustments, is shown in Table 2-1. Details of the inter-refinery transfer revenue are provided in Section 2.1. Other Board adjustments to the test-year revenue requirement are discussed in more detail in Chapters 3 to 6.

2.1 Inter-Refinery Transfer Revenue

Trans-Northern excluded from the determination of its revenue requirement inter-refinery transfer revenue derived from the use of the Montreal feeder system. This service is of a spot nature with the transfers only being made at times when the Montreal feeder system is not otherwise in use for regular service. The Company pointed out that the volumes transferred vary greatly from month to month and it declined to provide a test-year estimate of volumes.

In argument, Air Canada and Canadian Airlines International Ltd. (the Airlines) indicated that, based on the volumes transferred in 1986 and the toll of \$.55 per cubic metre (m^3) proposed by the Company, at least \$100,000 should be included in the determination of the test-year revenue requirement.

Decision

The Board finds the \$.55 per m^3 toll for inter-refinery transfers to be reasonable and believes that, as a matter of principle, revenue generated by regulated utility assets should be treated as a credit in the determination of the test-year revenue requirement. In the absence of a Company estimate of test-year volumes to be transferred, the Board has reviewed the actual test-year volumes from January to April and finds 90 000 m^3 to be a reasonable estimate for the test year.

Table 2-1

Revenue Requirement for the Test Year
($000)

	Application	NEB Adjustments	Authorized by NEB
Maintenance Expense	2,511	–	2,511
Transportation Expense	5,534	–	5,534
General Office Expense	4,242	–	4,242
Depreciation	1,918	–	1,918
Taxes Other Than Income Taxes	1,572	–	1,572
Income Taxes	3,561	(197)	3,364
Miscellaneous Items	765	–	765
Other Revenue	(25)	–	(25)
Inter-Refinery Transfer Revenue	–	(50)	(50)
Return on Rate Base	5,042	(191)	4,851
Revenue Requirement	**25,120**	**(437)**	**24,683**

Chapter 3
Rate Base

The Board's adjustments to rate base for the test year are summarized in Table 3-1. The details of the adjustments are explained in subsequent sections of this Chapter.

3.1 Method of Computing Rate Base

The Company used 13-point averages in its calculation of the test-year net transportation plant in service and working capital. This was in contrast to the use of a simple average of the opening and closing balances in the calculation of the test-year accumulated deferred income tax balance.

Decision

The Board continues to be of the view expressed in its 1985 Decision that the use of a 13-point average represents a more precise method of computation and has decided to employ it in computing all relevant rate base components.

3.2 Plant Additions to be Included in Rate Base

Decision

The Board has reviewed the Company's projected test-year additions to plant amounting to $2,082,000 and finds them to be acceptable for inclusion in the test-year rate base.

3.3 Working Capital

The Company followed the methodology used in the Board's 1985 Decision for the calculation of the allowance for working capital, with the exception that certain unamortized balances were included in the calculation of working capital. These unamortized balances related to debt issuance expenses ($56,000) and foreign exchange losses ($284,000).

Table 3-1

Rate Base for the Test Year
($000)

	Application	NEB Adjustments	Authorized by NEB
Net Transportation Plant in Service	43,486	–	43,486
Working Capital	2,051	(350)	1,702
Miscellaneous Deferred Items	–	340	340
Deferred Income Taxes	(9,019)	(5)	(9,024)
Rate Base	**36,518**	**(14)**	**36,504**

Decision

The Board has reviewed the Company's methodology of calculating working capital and, with the exception of the treatment of the unamortized balances, finds it to be acceptable.

The Board continues to be of the view expressed in its 1985 Decision that the unamortized balances relating to debt issuance expenses and foreign exchange losses should be removed from working capital and should be included in rate base as a separate category entitled Miscellaneous Deferred Items.

A summary of the approved working capital for the test year ending 31 December 1987, together with Board adjustments, is shown in Table 3-2.

3.4 Accumulated Deferred Income Taxes

Decision

The average accumulated deferred income tax balance to be deducted in computing the approved rate base is $9,024,000. Consistent with the Board's decision in Section 3.1, this balance has been calculated on a 13-point average basis (see Appendix V for the derivation of the approved deferred income tax balance). The computation of the test-year current deferred income taxes is shown in Table 3-3.

Table 3-2

Working Capital for the Test Year
($000)

	Application	**NEB Adjustments**	**Authorized by NEB**
Maintenance Expense	2,511	–	2,511
Transportation Expense	5,534	–	5,534
General Office Expense	4,242	–	4,242
Total Operating Expenses	12,287	–	12,287
Less:			
Municipal Property Taxes	1,462	–	1,462
Insurance Expense	535	–	535
Rental Expense	800	–	800
Add:			
Income Taxes Payable	3,257	(220)	3,037
Capital Taxes Payable	100	–	100
Net Cash Operating Expenses	**12,847**	**(220)**	**12,627**
Cash Requirement			
16/365 x Net Cash Operating Expenses	563	(10)	554
Prepaid Rent	194	–	194
Prepaid Insurance	218	–	218
Prepaid Municipal Taxes	164	–	164
Materials and Supplies	554	–	554
Oil Inventory	18	–	18
Unamortized Debt Issuance Expenses	56	(56)	-
Unamortized Foreign Exchange Losses	284	(284)	–
Working Capital	**2,051**	**(350)**	**1,702**

Table 3-3

Computation of Test-Year Current Deferred Income Taxes
($000)

	Application	NEB Adjustments	Authorized by NEB
Timing Differences			
Depreciation	1,918	–	1,918
Capital Cost Allowance	(2,515)	–	(2,515)
Amortization of Debt Issuance Expenses	22	–	22
Depreciation of Right-of-Way	(23)	–	(23)
Financing Expense –Proposed Issue	–	(45)[1]	(45)
Net Timing Differences	**(598)**	**(45)**	**(643)**
Income Tax Rate	.5083	.5083	.5083
Current Deferred Income Taxes (Net Timing Differences x Tax Rate)	**(304)**	**(23)**	**(327)**

1 In its application, the Company forecast debt financing expenses for 1987 of $45,000. This expense was omitted as a timing difference in the calculation of the test-year deferred income taxes.

Chapter 4
Depreciation and Amortization

The rates employed by the Company in arriving at the test-year estimate of depreciation expense were those approved by the Board in its 1981 Decision.

Decision

The Board has reviewed the Company's test-year estimate of depreciation and amortization expense in the amount of $1,918,000 and finds it to be reasonable.

Chapter 5
Cost of Capital

Trans-Northern applied for a rate of return on rate base of 13.81%. This compares to the currently approved rate of 14.46%. The applied-for capital structure, the corresponding individual cost rates and the overall requested rate of return are shown in Table 5-1.

5.1 Capital Structure

Consistent with past applications, Trans-Northern's applied-for capital structure represents its projected actual test-year capitalization. The applied-for debt and equity ratios of 48.77% and 51.23% respectively compare with the currently approved ratios of 49.29% debt and 50.71% equity. The common equity component of total capitalization was determined on a 13-point average basis; however, the applied-for long-term debt balances were determined on a 12-month average basis.

In his evidence, the Company's expert witness indicated that there had been two principal changes in business risk since the time of Trans-Northern's last toll hearing, both of which resulted in greater risk exposure. In this regard, the witness pointed to the relative increase in long-haul versus short-haul volumes and the fact that the Company was required to allocate space on its system in late 1986 and was forecasting it would have to do so again in the test year. The witness indicated that he did not view these risk increases to be substantial at this time, concluding that the Company's overall investment risks are not materially different as compared to 1985. In this vein, he stated that he did not regard the marginal increase in the common equity ratio as particularly significant.

With respect to the common equity component of the applied-for capitalization, the Company indicated that it proposed to pay out 100% of its 1987 earnings in the form of dividends, with the final installment expected to be paid on 31 December 1987. Trans-Northern stated that it did not reflect the expected year-end dividend

Table 5-1

Applied-For Average Capital Structure and Rates of Return for the Test Year

	Amount ($000)	Capital Structure (%)	Cost Rate (%)	Cost Component (%)
Funded Debt				
Three-Year	8,333	22.68	13.00	2.95
Three-Year	2,000	5.44	10.25	.56
Ten-Year	7,583	20.65	13.25	2.74
Total Debt Capital	17,917	48.77		6.25
Common Equity	18,821	51.23	**14.75**	7.56
Total Capitalization	36,738	100.00		
Rate of Return on Rate Base				**13.81**

payment in its equity component determination because the monies would not be available to the shareholders during the month of December.

Decision

The Board notes the Company's intention to pay out 100% of its earnings in the form of dividends during 1987, and its statement that the last dividend payment in 1987 is expected to be made at year end. The Board finds that it is proper to reflect this anticipated year-end dividend payment in the determination of the 13-point average common equity component of capitalization. Taking into account this decision, as well as the Board's findings with respect to long-term debt balances (see Section 5.2.2) and rate of return on equity (see Section 5.3), results in a capital structure of 49.08% debt and 50.92% equity. The Board finds this capital structure to be reasonable in light of the business risks faced by the Company.

5.2 Funded Debt

The Company's current long-term debt consists of \$10,000,000 in term notes due 30 October 1987 and \$10,000,000 in installment notes due 31 October 1994, with associated interest rates of 13% and 13.25% respectively. These rates were not at issue in this proceeding.

Trans-Northern's proposed debt re-financing and the question of the methodology used to determine the approved debt balances are discussed in more detail in Sections 5.2.1 and 5.2.2 respectively.

5.2.1 Cost of Proposed Debt Financing

The Company intends to re-finance its currently outstanding term loans in November 1987 with a \$12,000,000 issue under the same terms and conditions as the current issue, with the exception that the coupon rate associated with the new issue is expected to be 10.25%. In support of the applied-for rate, the Company sought comments from Dominion Securities Inc. (Dominion Securities), which has in the past acted as an agent in arranging financing for Trans-Northern. Dominion Securities submitted its forecast that mid-term Government of Canada bonds would yield 9.1% at the end of September 1987, and that the spread above such debt for a private placement by a credit similar to Trans-Northern, under current market conditions, would be 1.125 to 1.25 percentage points. Taking into account the potential for rising interest rates, Dominion Securities was of the opinion that the cost to the Company of three-year, fixed-rate financing in September 1987 would be at least 10.25%.

Decision

The Board recognizes that Dominion Securities has previously acted as an agent for the Company in arranging financing and, as such, is familiar with its operations and creditworthiness. There was no evidence to suggest that a cost rate of 10.25% is unreasonable under the current economic circumstances. The Board approves a cost rate of 10.25%.

5.2.2 13-Point Average Debt Balances

In its application, Trans-Northern computed rate base and the common equity component of total capitalization using 13-point averages; however, it determined the outstanding debt balances on a 12-month average basis. This methodology does not conform to the Board's 1985 Decision, where it was decided to employ 13-point averages in computing both the approved debt and equity balances.

The Company was of the view that its method of determining the long-term debt balances in this proceeding was more appropriate, after having taken into account the different debt issues involved, together with the different interest rates and terms of the various debt instruments.

Decision

The Board was not persuaded by the Company's statements that it is more appropriate to calculate debt balances using a 12-month average. The Board continues to believe that the long-term debt balances should be determined in a manner consistent with that used to determine rate base and the common equity component of total capitalization. Accordingly, the Board has re-calculated the Company's debt balances on a 13-point average basis (see Appendix V for the derivation of the approved debt balances).

5.3 Rate of Return on Equity

In its application, Trans-Northern applied for a rate of return on equity of 14.75%, as compared to

the currently approved rate of 15.75%. In support of the applied-for rate, the Company relied on the advice of its expert witness. The Company's witness concluded that the fair rate of return on equity for Trans-Northern was in the range of 14.5% to 15%, further suggesting that 14.75% be considered the minimum rate in recognition of the comparative risk of Trans-Northern and the high-quality, unregulated companies in his samples. In arriving at his recommendation, the witness employed the comparable earnings, discounted cash flow (DCF) and equity risk premium approaches in estimating the cost of equity capital.

In reaching his conclusion that a fair rate of return on equity for Trans-Northern was in the range of 14.5% to 15%, the witness placed primary emphasis on the results emanating from his comparable earnings analysis. This witness examined the returns on book equity for four groups of high-quality, low-risk unregulated companies. After examining the historical returns earned by these groups for the periods 1979 to 1985, 1982 to 1985 and 1983 to 1985, he opined that the prospective earnings for such companies in 1987 would be in the range of 14.5% to 15%. He concluded that, based on his assessment of Trans-Northern's investment risks, the fair rate of return on equity indicated by this test was at least 14.75%.

With respect to his DCF analysis, the witness utilized a dividend yield of 2.25% to 2.5% and a growth factor of 10.5% to 10.75%, concluding that the investors' required rate of return on common equity for his sample companies was approximately 13%. He then determined that this rate would have to be adjusted upwards to a level of 13.6% to 14.2% in order to permit the Company to undertake new equity financing without diluting existing equity. This range implies the use of a market-to-book ratio of 1.1 to 1.2. The witness placed emphasis on the upper end of this range in recognition of the fact that the current market-to-book ratios for his sample companies are considerably higher than the 1.2 level implicit in the 14.2%.

In his equity risk premium analysis, the Company's witness examined the results of three studies in order to determine the appropriate risk premium to add to his forecast long-term Government of Canada bond (long-Canada) rate of 8.75% to 9.25%, or 9% on average. This forecast compares to the estimated long-Canada rate of 11.25% to 12.25% utilized by the same witness at the Company's last toll hearing. He concluded in this instance that a range of 3.75 to 4.5 percentage points was a reasonable estimate of the required risk premium, resulting in an investors' required rate of return range of 12.75% to 13.5%. He viewed an investors' required rate of return range of 13% to 13.25% as a minimum in light of the risks to which Trans-Northern is exposed. Adjusting this range to reflect a market-to-book ratio of 1.1 to 1.2 resulted in a rate of return on equity range of 13.6% to 14.5%, with the witness again placing greater reliance on the upper end of the range because the current market-to-book ratios for his sample companies are higher than the 1.2 level implicit in the 14.5%.

The Airlines, while not presenting expert evidence, argued that approval of the applied-for rate of return on equity of 14.75% would not reflect current and prospective conditions, stating that a further and substantial reduction from the currently authorized rate was necessary in order to arrive at tolls that would be just and reasonable.

Decision

The Board notes that the Company's witness placed greatest reliance on the results of his comparable earnings analysis. The Board is of the view that increasing or decreasing rates of inflation can significantly affect the applicability of the results of the comparable earnings test. In selecting comparable risk companies, the Board notes the Company witness's extensive use of stock rankings, which are in part dependent on the experienced level of earnings. This practice may favour the selection of traditionally high earners. For these reasons, the Board has placed less reliance on the results of the comparable earnings test in this proceeding.

With respect to investment risk, the Board is of the view that there has not been a significant change for Trans-Northern since the time of the Company's last toll hearing. The Board notes that the Company's witness continues to hold the view that Trans-Northern's investment risks are greater than those of Interprovincial Pipe Line Limited. The Board concurs with this assessment.

In addition, the Board notes that the long-Canada rates forecast in this proceeding are 275 basis points lower, on

average, than they were at the time of the Company's last toll hearing. The Board is of the view that the recently forecast rates for long-Canada's represent a clear signal that the cost of capital is currently much lower than at the time of the last toll hearing.

The determination of a fair rate of return on equity requires the exercise of judgment. Having considered the evidence of this case, giving particular consideration to the investment risks faced by Trans-Northern relative to other companies, the reduction in interest rate forecasts since the time of the Company's last toll hearing, and the prospect for such rates, the Board finds 13.75% to be a fair and reasonable rate of return on equity.

5.4 Rate of Return on Rate Base

Decision

Based on its findings in this case, the Board has approved a rate of return on rate base of 13.29% for the test year. The approved capital structure and the derivation of the allowed rate of return are shown in Table 5-2.

5.5 Income Taxes

5.5.1 Income Tax Rate

Trans-Northern used an overall tax rate of 50.83% in computing its test-year income tax provision. This rate is comprised of a federal corporate tax rate of 35.5%, a composite provincial tax rate of 14.26% and an effective federal corporate surtax rate of 1.07%.

Decision

The Board accepts the use of an overall tax rate of 50.83% for the purpose of calculating Trans-Northern's test-year income tax provision.

5.5.2 Normalized Tax Calculation

Consistent with past applications, the Company calculated its test-year income tax provision using the normalized method. The continued use of this approach was not at issue in this proceeding.

Table 5-2

Approved Average Capital Structure and Rates of Return for the Test Year

	Amount[1] ($000)	**Capital Structure** (%)	**Cost Rate** (%)	**Cost Component** (%)
Funded Debt				
Three-Year	8,462	23.17	13.00	3.01
Three-Year	1,846	5.06	10.25	.52
Ten-Year	7,615	20.85	13.25	2.76
Total Debt Capital	17,923	49.08		6.29
Common Equity	18,595[2]	50.92	**13.75**	7.00
Total Capitalization	36,518	100.00		
Rate of Return on Rate Base				**13.29**

1 The derivation of the individual 13-point average capitalization amounts is shown in Appendix V.

2 Adjusted to reflect the Board's decisions in Sections 5.1, 5.2.2 and 5.3.

Decision
The Board considers the continued use of the normalized method to be appropriate. As a result of its decisions in this case, the Board has adjusted the normalized income tax provision from $3,561,000 to $3,364,000, a reduction of $197,000 (see Table 5-3).

Table 5-3

Approved Income Tax Provision for the Test Year
($000)

	Application	NEB Adjustments	Authorized by NEB
Utility Income After Tax	2,749	(191)	2,558[1]
Add (Deduct) Permanent Differences			
Eligible Capital	(22)	–	(22)
Non-Deductible Miscellaneous	20	–	20
Depreciation of Right-of-Way	23	–	23
Loss on Foreign Exchange	568	–	568
Assets in "Other Plant" Retired	107	–	107
Normalized Income After Tax	**3,445**	**(191)**	**3,254**
Normalized Income Tax provision2	**3,561**	**(197)**	**3,364**

1 Equals allowed return on rate base less forecast actual interest expense ($4,851,000 - $2,293,000)

2 Equals normalized income after tax multiplied by the tax rate divided by (1 - tax rate).

Chapter 6
Operating Costs

In its test-year estimate of operating expenses, the Company projected increases for inflation in non-labour expenses of 4% and in labour expenses of 3%. A summary of the expenses is shown in Table 6-1.

Decision

The Board has reviewed the Company's estimate of operating costs for the test year and finds them to be reasonable.

Table 6-1

Operating Costs Applied-For by the Company and Authorized by NEB
($000)

Maintenance Expense		
Labour	1,090	
Non-Labour	1,421	2,511
Transportation Expense		
Labour	1,743	
Non-Labour	3,791	5,534
General Office Expense		
Labour	1,428	
Non-Labour	2,814	4,242
Taxes Other Than Income Taxes		1,572
Miscellaneous Items		765
Other Revenue		(25)
Total Operating Costs		**14,599**

Chapter 7
Throughput

Trans-Northern submitted a throughput forecast of 8 166 000 cubic metres for the test year 1987. This forecast is seven percent below the throughput volume approved by the Board for the 1985 test year and two percent below the actual throughput achieved in 1986.

During the Company's last toll hearing, the sourcing of deliveries to Ottawa was the major issue raised in connection with throughput. Deliveries to Ottawa can be sourced from either the Montreal or Toronto areas. It was assumed that for the test year 1985 Ottawa would receive 75% of its deliveries from Montreal and the balance from Toronto. For 1987, Trans-Northern believes 62% of the petroleum products it will move to Ottawa will originate in the Toronto area and the rest from Montreal. This reflects the 1986 experience when 60% of Ottawa deliveries were sourced from Toronto. No intervenor raised any concern over Trans-Northern's estimate of supply to Ottawa in 1987.

The principal matter raised with respect to throughput during the review of this application involved the forecast of deliveries to the three airports on Trans-Northern's system, namely the Dorval International Airport (Dorval) and Mirabel International Airport (Mirabel) in the Montreal area and the Lester B. Pearson International Airport (Pearson) in Toronto. The Airlines submitted a forecast of deliveries for 1987 to the three airports that was somewhat higher than that provided by Trans-Northern, as indicated in Table 7-1.

Trans-Northern subsequently indicated that it was prepared to accept the Airlines' estimates for Dorval and Mirabel.

Decision

The Board finds that the Airlines' estimates of deliveries to Dorval and Mirabel are reasonable and notes that they were acceptable to Trans-Northern. However, the Board is not persuaded that the Airlines' forecast for Pearson is superior to that of Trans-Northern.

Accordingly, based on the evidence before it in this matter, the Board approves a throughput forecast of 8 194 000 m^3 for the test year 1987. The breakdown of deliveries therein is as filed by Trans-Northern, with the exception of the deliveries to Dorval and Mirabel where the forecasts submitted by the Airlines are accepted.

Table 7-1

Forecast of 1987 Deliveries
(Thousands of Cubic Metres)

	The Airlines	Trans-Northern	Difference
Dorval	228[1]	215	13
Mirabel	422	407	15
Pearson	599	552[2]	47

1 Revised from 293 000 cubic metres

2 Includes the amount for the Toronto Airport Junction of 24,000 cubic metres.

Chapter 8
Toll Design

Trans-Northern has designed the tolls for the test year in accordance with the principles approved in the Board's 1985 Decision. The allocation of average rate base and return on rate base for toll design purposes and the allocation of the revenue requirement are shown in Appendices III and IV respectively.

8.1 Inter-Refinery Transfer Toll

Decision

The Board has reviewed the Company's allocation of the inter-refinery transfer toll between the lifting and delivery components and finds it to be reasonable.

8.2 Determination of Tolls

The Board has approved a revenue requirement of $24,683,000 and a throughput forecast of 8 194 000 m^3 as the basis for determining the tolls.

The details of the tariff components, as applied for, along with the adjustments which are as a result of Board decisions previously discussed in this Decision, are shown in Table 8-1.

Decision

The Board finds that the tolls contained in Schedule "A" of Appendix 1 are just and reasonable and directs that these tolls be charged effective 1 September 1987.

8.3 Refund to Shippers

By Board Order No. TOI-1-87, the existing tolls were made interim effective 1 February 1987 pending a final determination of Trans-Northern's tolls.

Decision

The Board directs Trans-Northern to refund to each shipper who shipped refined petroleum products during the period 1 February to 31 August 1987:

(1) the difference between the revenues from volumetric tolls collected from that shipper for that period and the revenues that would have been collected from that shipper for that period based on the volumetric tolls set out in Schedule "A" of Appendix I; and

Table 8-1

Tariff Components for the Test Year
(in cents)

	Application	NEB Adjustments	Authorized by NEB
Lifting (per m^3)	22.7540	(0.7739)	21.9801
Transmission (per m^3km)	1.1307	(0.0184)	1.1123
Delivery (per m^3)	32.7131	(0.7426)	31.9705
Airport Terminals (per m^3)			
Pearson	97.6550	(1.6609)	95.9941
Dorval	139.9383	(9.5636)	130.3747
Mirabel	97.7535	(5.2165)	92.5370

(2) the interest on each monthly component of the refund for the period from the date of the invoice under which that component was originally collected to the date of the refund, at the rate per annum charged Trans-Northern from time to time during the period by its bank for short-term loans.

The refund is to be applied as a credit to the September 1987 billing of each shipper who is entitled thereto except that if a shipper does not ship in September 1987, Trans-Northern shall remit to that shipper, no later than 16 October 1987, the refund to which he is entitled. If a shipper's September 1987 billing is less than the refund to which he is entitled Trans-Northern shall remit to that shipper, no later than 16 October 1987, the difference between the refund to which he is entitled and his September 1987 billing.

Chapter 9
Disposition

Order No. TO-3-87, which is presented as Appendix I, is based upon these Reasons for Decision. The foregoing, together with the above-noted Order, constitute our Reasons for Decision and our Decision on the application by Trans-Northern Pipelines Inc.

R.F. Brooks
Presiding Member

J.R. Jenkins
Member

R.B. Horner, Q.C.
Member

Ottawa, Canada
July 1987

Appendix I

ORDER NO. TO-3-87

IN THE MATTER OF the National Energy Board Act (the Act) and the Regulations made thereunder;

AND IN THE MATTER OF an application by Trans-Northern Pipelines Inc. (hereinafter called "Trans-Northern" or "the Company") for an order respecting tolls pursuant to Part IV of the Act, filed with the Board under File No. 1762-T2-9.

BEFORE:

R.F. Brooks
Presiding Member

J.R. Jenkins
Member

On Thursday, the 9th day of July 1987.

R.B. Horner, Q.C.
Member

WHEREAS the Board, by Order No. TOI-1-87 dated 21 January 1987, approved interim tolls effective 1 February 1987 for the transportation of refined petroleum products by Trans-Northern and further directed the Company to file certain cost of service, throughput, rate of return and income tax information;

AND WHEREAS, pursuant to Section 50 of the Act, Trans-Northern filed an application dated 11 March 1987 for an order fixing the just and reasonable tolls the Company may charge for or in respect of the transportation of refined petroleum products;

AND WHEREAS the Board decided to proceed by written submission for the consideration of the application, the written submission procedure being set out in Order No. RH-3-87;

AND WHEREAS the Board has considered the application, and the evidence and arguments relative to the application submitted by Trans-Northern and interested parties;

AND WHEREAS the Board's decisions on the application are set out in its Reasons for Decision dated July 1987 and in this Order;

IT IS ORDERED THAT:

1. Subject to paragraph 2, Trans-Northern shall, effective 1 September 1987, charge for or in respect of the transportation of refined petroleum products the tolls prescribed in Schedule "A" attached hereto.

2. (1) Trans-Northern shall refund to each shipper who shipped refined petroleum products during the period beginning 1 February 1987 and ending 31 August 1987

   (a) the difference between the revenues from volumetric tolls for the transportation of refined petroleum products collected from that shipper during the period beginning 1 February 1987 and ending 31 August 1987 and the revenues that would have been collected from that shipper based on the volumetric tolls set out in Schedule "A" attached hereto; and

   (b) interest on each monthly component of the amount referred to in subparagraph (a) for the period from the date of the invoice under which that component was originally collected to the date of the refund required by subparagraph (a), at the rate per annum charged Trans-Northern from time to time during the period by its bank for short-term loans.

   (2) The refund provided for in subparagraph (1) shall be applied as a credit to the September 1987 billing of each shipper who is entitled thereto except that

   (a) if a shipper does not ship in September 1987, Trans-Northern shall remit to that shipper, no later than 16 October 1987, the refund to which it is entitled; and

(b) if a shipper's September 1987 billing is less than the refund to which it is entitled Trans-Northern shall remit to that shipper, no later than 16 October 1987, the difference between the refund to which it is entitled and its September 1987 billing.

3. The Company shall forthwith file with the Board a tariff conforming with the Board's Reasons for Decision dated July 1987 and this Order and serve it upon:

   (1) the Company's shippers;

   (2) the Attorneys General of Ontario and Quebec;

   (3) all intervenors to the above-mentioned proceeding; and

   (4) any person who notifies the Company and the Board that he wishes to be registered as an interested person in the Company's tolls and tariffs, and is accepted by the Board as such.

4. Notwithstanding the filing of the new tariff referred to in paragraph 3, the same shall not come into effect until 1 September 1987.

5. The provisions of Trans-Northern's tariff or any portion thereof that are contrary to any provision of the Act, to the Reasons for Decision dated July 1987 or to any order of the Board including this Order, are hereby disallowed after 31 August 1987.

NATIONAL ENERGY BOARD

J.S. Klenavic
Secretary

SCHEDULE "A"

Trans-Northern Pipelines Inc.
Tolls Effective 1 September 1987 in
Dollars Per Cubic Metre

Points of Origin

Destination	Montreal East Quebec	Nanticoke Ontario	Oakville Ontario	Clarkson Ontario	North Toronto Ontario	Toronto Airport Junction Ontario
Montreal, Quebec		8.080	7.195	7.034	6.592	
Dorval, Quebec (Jet)	1.980	9.521	8.635	8.475	8.033	
Dorval, Quebec (Non-Jet)	0.996	8.537	7.651	7.491	7.049	
Mirabel, Quebec	1.660	9.200	8.315	8.155	7.713	
Cornwall, Ontario	1.875	6.744	5.859	5.698	5.257	
Prescott, Ontario	2.713	5.970	5.085	4.924	4.482	
Maitland, Ontario	2.853	5.766	4.881	4.720	4.278	
Ottawa, Ontario	2.910	7.223	6.338	6.177	5.735	
Kingston, Ontario		4.792	3.907	3.746	3.305	
Belleville, Ontario		4.029	3.144	2.983	2.542	
Port Hope, Ontario		3.159	2.274	2.113	1.671	
Markham, Ontario		2.257	1.372	1.212	0.770	
Toronto Harbour, Ontario		2.349	1.463	1.303	0.861	
North Toronto, Ontario		2.027	1.142	0.981		
Toronto Airport, Ontario		2.553	1.668	1.508		1.216
Clarkson, Ontario		1.585	0.725			
Oakville, Ontario		1.425		0.725		
Hamilton, Ontario		1.214				

Appendix II

Calculation of Income Taxes Payable
Included in Cash Working Capital
($000)

Final Iteration of Rate Base			
Average Net Plant in Service			43,486
Average Accumulated Deferred Income Taxes			(9,024)
			34,462
Working Capital			
Total Operating Expenses	12,287		
Less: Municipal Property Taxes	1,462		
Insurance Expense	535		
Rental Expense	800	9,490	
Add: Income Taxes Payable		3,037	
Capital Taxes Payable		100	
Net Cash Operating Expenses		12,627	
Cash Working Capital (16/365 x 12,627)		554	
Material and Supplies		554	
Prepaid Rent		194	
Prepaid Insurance		218	
Prepaid Municipal Taxes		164	
Oil Inventory		18	1,702
Miscellaneous Deferred Items			
Unamortized Debt Issuance Expenses		56	
Unamortized Foreign Exchange Loss		284	340
Average Rate Base			**36,504**

Calculation of Income Taxes Payable
Included in Cash Working Capital
($000)

Final Iteration of Income Taxes Payable

Return on Rate Base (.1329 x 36,504)	4,851	
Less: Interest Expense	2,293	
Utility Income After Tax	2,558	
Add (Deduct) Permanent Differences		
Eligible Capital	(22)	
Non-Deductible Miscellaneous	20	
Depreciation of Right-of-Way	23	
Loss on Foreign Exchange	568	
Assets in "Other Plant" Retired	107	3,254
Normalized Income Tax Provision		
$3{,}254 \times \frac{.5083}{1 - .5083}$		3,364
Add (Deduct) Timing Differences		
Depreciation	1,918	
Capital Cost Allowance	(2,515)	
Amortization of Debt Issuance Expenses	22	
Depreciation of Right-of-Way	(23)	
Financing Expense–Proposed Issue	(45)	(643)
Taxable Income		**5,974**
Income Taxes Payable (5,974 x .5083)		**3,037**

Appendix III

Functional Allocation of Rate Base and Return on Rate Base for the Test Year
($000)

	Lifting	Trans-mission	Delivery	Pearson Airport	Dorval Airport	Mirabel Airport	Total[1]
Net Transportation Plant in Service	4,134	34,518	2,456	1,049	445	884	43,486
Working Capital	162	1,351	97	41	17	34	1,702
Miscellaneous Deferred Items	32	270	19	8	3	7	340
Deferred Income Taxes	(857)	(7,165)	(514)	(217)	(90)	(180)	(9,024)
Rate Base	**3,471**	**28,974**	**2,058**	**881**	**375**	**745**	**36,504**
Return on Rate Base	**461**	**3,851**	**273**	**117**	**50**	**99**	**4,851**

1 Board-allowed amounts have been allocated in the same proportions as the amounts contained in the Company's application.

Appendix IV

Functional Allocation of Revenue Requirement for the Test Year
($000)

	Lifting	Trans-mission	Delivery	Pearson Airport	Dorval Airport	Mirabel Airport	Total[1]
Operating Expenses	895	11,328	1,710	289	187	191	14,599
Depreciation	145	1,580	92	43	26	32	1,918
Return	461	3,851	273	117	50	99	4,851
Income Taxes	320	2,670	190	81	35	69	3,364
Inter-Refinery Transfer Revenue	(20)	–	(29)	–	–	–	(50)
Total Revenue Requirement	**1,801**	**19,429**	**2,235**	**530**	**297**	**391**	**24,683**
Cubic Metres	8 194 000	–	6 992 000	552 000	228 000	422 000	
Cubic Metre-Kilometres (000)		1 746 760[2]					
Tariff Component (in cents)	21.9801	1.1123	31.9705	95.9941	130.3747	92.5370	

1 Allowed totals have been allocated in the same proportions as the amounts contained in the Company's application

2 Board computation based on the authorized throughput forecast

Appendix V

Calculation of 13-Point Averages for Accumulated Deferred Income Taxes, and Debt and Equity Capital
($000)

1987	Accumulated Deferred Income Taxes[1]	Common Equity[2]
January 1	8,867	18,398
January 31	8,894	18,611
February 28	8,920	18,825
March 31	8,947	18,398
April 30	8,973	18,611
May 31	8,999	18,825
June 30	9,025	18,398
July 31	9,049	18,611
August 31	9,074	18,825
September 30	9,099	18,398
October 31	9,123	18,611
November 30	9,147	18,825
December 31	9,194[3]	18,398
Total	**117,312**	**241,734**
13-Point Average	**9,024**	**18,595**

1 Reflects the Company's response to question 7 of the Board's first information request dated 27 April 1987.

2 Adjusted to reflect the Board's decisions in Sections 5.1, 5.2.2 and 5.3.

3 Adjusted to reflect the Board's determination of the test-year deferred income taxes of $327,000 (see Section 3.4).

Calculation of 13-Point Averages for Accumulated Deferred Income Taxes, and Debt and Equity Capital
($000)

Long-Term Debt[1]

	3-year		10-year
1987	**13%**	**10.25%**	**13.25%**
January 1	10,000	–	8,000
January 31	10,000	–	8,000
February 28	10,000	–	8,000
March 31	10,000	–	8,000
April 30	10,000	–	8,000
May 31	10,000	–	7,500
June 30	10,000	–	7,500
July 31	10,000	–	7,500
August 31	10,000	–	7,500
September 30	10,000	–	7,500
October 31	10,000	–	7,500
November 30	–	12,000	7,000
December 31	–	12,000	7,000
Total	**110,000**	**24,000**	**99,000**
13-Point Average	**8,462**	**1,846**	**7,615**

1 Adjusted to reflect the Board's decision in Section 5.2.2.